

Money and Banking
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Lecture – 39

What I am going to start today is the cooperative banks its amazing these institutions. Now there are some books coming up some books are there, when I was a student, I got a couple of books, they are very different kinds of institutions, they are not corporate companies. Banks are corporate companies; cooperative banks are not corporate companies, they are very different and they come under something called cooperative societies and you must have heard that cooperative societies are all around us. You must have heard of cooperative housing society; you must have heard cooperative housing society. Then, if you go to rural or semi urban areas of India, you will find cooperative stores, selling goods. Urban area [FL], rural a semi urban area [FL] India [FL], you will find cooperative stores - selling goods, all kinds of goods.

Now let me tell you about the cooperative society, I will go very slowly initially at least. Essentially the idea of cooperative institution, I think it has come from the east European or Russian USSR it has to be known. It is found is an intuition founded by a group of individuals, like we - four, five, ten of us can get together and form a cooperative society, for whatever purpose. It may not be a bank; it may be something else like housing society; like a shop, open a shop or educational institution who knows. And we form it and we are not called share holders, this is like a society. So, there are members, so we will be called members of the society. So, it is no share capital as such alright initially, this is a philosophical understanding of a cooperative society. There is a philosophical base for a constitution, the parliament, the political party, what they meant to do.

Cooperative society is interesting enough have a philosophical base. It says that it works on the operates on the principal of cooperation. So, we cooperate each other, we not compete; we do not compete, we cooperate each other. So, if you cannot do something, I would help you; I cannot do something, you would help me. It is not if you cannot do something, so I tried to bypass you and go ahead in the race, competition [FL] self-help

which implies self-help; now in India today, we have central government, self help organization schemes etcetera also.

Self-help, basically to help your selves. So, you form a society to help yourself; a housing society, what it means? A group of people get together from a housing society, essentially they would all pull their money together; appoint a contractor and build the house, and say ten people ten flats, and it is called a cooperative housing society and where they would look after the housing society, the maintenances etcetera alright. So, cooperation not competition, self help and mutual help and it is the same thing. You help yourself, you would help each other and we cooperate. So, there is no profit motive as such, the basic point am going to derive is very unlike the competitive society. There is no profit motive here.

Now in India if you look at the cooperative society around you will find their cooperative society is in production activities, in processing activities, food processing, other processing activities, marketing, distribution, servicing, banking, all sorts of areas cooperative societies exist. Now in India cooperative banking gets back to 1904, the history says the earliest cooperative bank was found, I found this information in professor Bhole's first edition of the book thin book it is in the library. We had a chapter on cooperative bank its very interesting little chapter, but very useful very informative. So, 1904 the first cooperative bank was founded and this where created in rural areas with the purpose which is very understandable they where no banking system what so ever those days. Commercial banks never whoever existed like State Bank of India then had the name imperial bank of India; it never had a branch there.

Few rural areas the only sources of fund was these very notorious money lenders, and they where you know in their grip and they want to find an alternative financing institution and then found the cooperative society that is how it started in rural India not in urban areas. Whether credit was very inadequate and private lenders is use to lend money and they still do at the very high interest rate. Now, you have so many institutions you just have a cooperative society, you heard about rural banks, visual rural banks you have commercial bank branches you have NABARD sometimes walking directly, so I will talk about NABARD, NABARD role here very important cooperative banks.

So, like commercial banks however, it has some sort, it is not a share holding company in that sense, but they have modern cooperative banks do have some subscription do share capital I have heard. But initially the concept was not share capital the members who pool their money whatever you have whatever I have pool together and that remains as pool of resources out of which if you need the money today I will lend you then you return then he gets the money his turns comes he borrows. When he returns then the other person, borrow just like self-help groups they are developing in India today.

Now, but like commercial banks it has very some similarity when it comes to banking, it actual deposits there money own money is not sufficient they ask people to open accounts, supply credit both short term and long term, very interesting loans etcetera they gave. I do not think, they have a cash credit system, they have a loan system; short term and long-term loans they give. And they also provide remittance facilities, so you want to send money to your brother somewhere else he is residing you can send money - remittance facilities, you can remit funds. So, it is very much there some activities of this cooperative banks which are very similar to commercial bank activities.

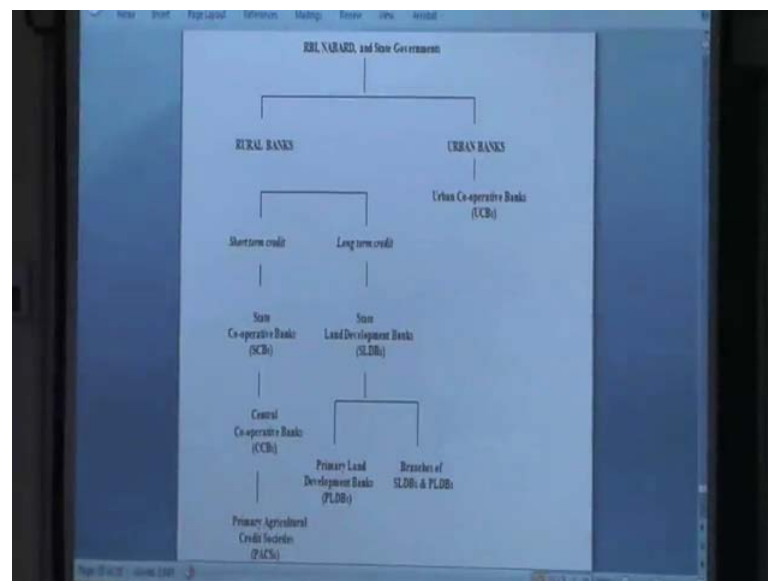
Now some of this banks also these days the big banks, big cooperative banks provide housing loans which means lakhs of rupees, not small farmer's loan – 10000, 5000, 20000; lakhs of rupees housing loans. They also provide some times advances again shares and debentures [FL] cooperative banks they give advance again share and debentures which will be used as some sort of collateral. So, they are offer various kinds of services commercial banks, but it is not as wide as commercial banks commercial banks have diversified immensely in the past twenty-thirty years. Commercial banks have mutual fund companies, commercial banks have venture capital firms, commercial banks have also of investment activities in government and non-government bonds etcetera; commercial banks are going to discounting of commercial bills; they go into C p market and finance they go have C d, they various kinds of fixed deposits. So, commercial bank activities are enormous; some of the commercial bank are also open subsidiaries who are under writers.

ICICI [FL] ICICI was a is a industrial development finance [FL] IDBI [FL] created [FL] in the private sector. IDBI was a government created intuition, ICICI was primary a world bank created institution basic difference. Look what ICICI has today, it has a ICICI prudential insurance business [FL]. ICICI bank in commercial bank business

[FL].They have ICICI capital or something they are into under writing of shares. They have many they have diversified. Now commercial banks cooperative banks are not that big not diversified at all; they go into basic banking activities; accept deposits, provide remittance facilities, provide loans to the members primarily that what they do etcetera.

So, cooperative banks through mutual funds, venture capital fund companies they do not participate in the repo market, they do not have a call market to help each other, they do not have any of this other things that you have learned so far. I will give you my notes whatever I have. Now before I go into the detail understanding of how cooperative banks function in India, I have to show you a tree - cooperative bank tree it is a classification of various kinds of cooperative bank that exist. Niketan would you please pass this one, I forgot. I will have to tell about the cooperative bank tree. Now here is the tree, I will bring my laptop every day to show this to you. This is a structure of cooperative; at the top you have RBI, NABARD, and State governments. These are the controlling funding regulatory authorities; cooperative bank do not just have a RBI controlling them.

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Cooperative banks are controlled by NABARD and largely by state governments. So, every state government has the cooperative department and that cooperative department issues the license to form a cooperative society which is called the registration. If you form a society, it has to be registered; you will have a registration number. Now where you get that? You do not go to Bombay stock market, you do not go to company board,

you go to the cooperative department of the state government, every state has that. In fact, they have ministry in charge of cooperative society also. They have may be other portfolios, but cooperatives activities society activities is one of the responsibilities and this department issues the license or provide the registration, if you form tomorrow you may be requiring to do get a cooperative society form.

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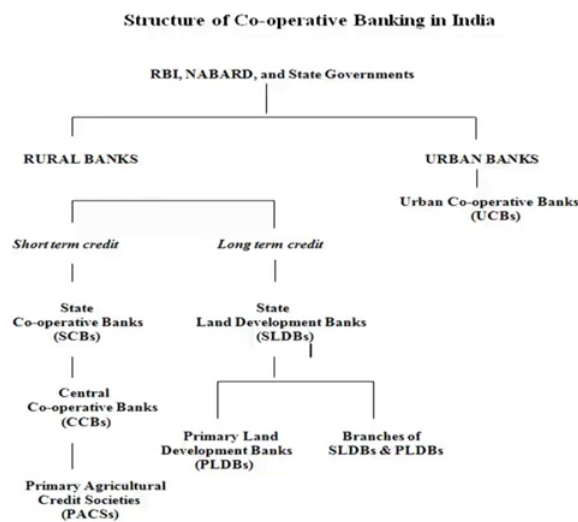


Figure V.20

Now, look at the cooperative banks here. There are two kinds rural banks, urban banks. Urban banks they have simple one type of banks they are called urban cooperative banks UCBs. Rural bank [FL] cooperative moments started in India banks is very complex. In rural, you have short term credit a particular type of cooperative organizations, your long term credit another kind of cooperative banks they are know technically speaking. In the short-term credit, the first branch you have the state cooperative banks every state has the state cooperative bank under the state you have the districts. So, you have the central cooperative banks operating at the district level [FL]. So, every state has a state cooperative bank like a mother organization under the state cooperative bank you have the central cooperative banks at a district level.

Within the district, you have the villages, panchayats, etcetera, blocks, wards, villages etcetera. Wards in urban areas, blocks and villages and then at the village level what you have after the district you have what you call PACs - primary agricultural credit societies, PACs. You have the PACs s - primary agricultural credit societies, these are

the intuitions, who are the real cooperative banks, because they are in touch with the borrower. So, now, what happens at the district level banks like central cooperative banks, and what happens at the state level banks for each state there is at least one.

Sometimes I have heard some state level cooperative banks also go beyond the state jurisdiction say the state level cooperative bank in West Bengal may have some area under its operation in Bihar. Because also you have to understand that the states got created and rearranged in last 50-60 years continuously or even before that. So, their operations are not that what are tied within the state, but every state has a state government and under the state districts should have one central cooperative bank. Then under the central cooperative banks, you have the actual cooperative bank to do the business who lend the loan, give you the money the farmers etcetera, they are called primary agriculture credit societies.

Now if you go into the long term credit, you have again state land development banks they call SLDBs. State land development banks, in long term credit your state land development banks in long term credit SLDBs then at the district level and the village level what you have primary and development banks in the village level. And at the village level also, you have branches of state land development banks and primary land development banks. The one thing you notice here there is no district level distinction here level straight from the state level land development banks, you go directly to the village level where you have primary land development level banks and branches of state land development banks. Whereas, in the first branch there you see state level you have state cooperative banks, district level you are central cooperative banks village level your primary agriculture credit societies no branch word is mention.

So, these banks what are known as unit bank types, rural credit [FL], they are unit bank types. Unit means what one bank one society somebody found it it does not have branch. But in case of land development banks, it is like our commercial banks, state bank has a branch in Kanpur, state bank has a branch in (()), state bank have couple of branch within other parts of Kanpur city state bank have branches all over India. Very different, they are branch banking type, they are called branch banking type. The land development the long term credit branch credit branch banks. Whereas, in case of rural credit, is very much a unit banking type conceptual speaking, they are called unit banks; that means,

one cooperative society is one bank found by group of individuals who do not necessarily control the other one, there is another one.

Next village has another cooperative society, another bank; completely difference out of the people or members. But in case of long term credit, their branches and both primarily land development bank as well as state land development bank remember that, they are not unit bank type, this is very important distinction.

Now let me tell you this is highly this is hardly what I have said anything except just giving you birds eye view of how the cooperative banks in India are conceptually classified. Now I come to the operational part. It is very interesting, how they operate. The distinctive feature of cooperative banks that I have just shown you are as follows. They are in the rural economy. So, serving agriculture mostly and some of them do also serve agro based industries today. Fruit processing, fruit processing is becoming a very important then horticulture, some industries are developing a lot. Horticulture means they are trying to developing so much that they are trying to export flower also unbelievable, just a food processing. Food processing includes all kinds of food, but they are also into horticulture and various other things.

Now if you look into the entire structure of cooperative banks in India today, they are of the mix type. Some are unit-banking type, some are branch banking type, there are mix type. Commercial bank; however are all one type, they are called branch banking type, but they are not. But I have doubt something about regional rural bank whether they have branches they may or may not I am not very clear. Now there was an important email that has come over CRR money where there was an interest given by RBI who sent it to me that is a very interesting point, they changed it.

So, what they doing RBI there is a digression I am having here what RBI is doing. RBI saying if you keep my CRR money, which you have to keep by law, but you would not get interest means basically asking them to perform in better I mean that do not type CRR [FL] interest [FL] deposit money[FL] deposit it as you and me. But they have change that it seems to be. So, there is no interest on CRR basically forcing banks to perform even better because whatever money remains with you now try to make money on that, so that you can earn money for yourself, you can pay the depositor's interest and whatever. And also manage your m p a's is essential a performance enhancing measure,

they have taken. RBI would by law collect CRR cash not paying an interest on it, which they used to. And what his email said which I forwarded to all of you not in group the other people the Email said that I haven't read the I could not open the link basically what he saying is no interest paid these days on CRR by RBI.

I am coming to some of these things here. So, these is the business this semi urban, urban and metropolitan cities also have urban banks, cooperative banks etcetera. So, they are mix banking type. As I told you the state credit bank, state cooperative bank, central cooperative bank and primary agriculture credit societies are mostly of the unit banking type. Whereas a land development bank in case of long term credit either the primary land development banks or the state land development banks, they are of the branch bank type. Cooperative banks do not create credit, very important point commercial bank do, very important point. So, they cannot collect this amount of money like hundred crores or say hundred thousand or one lakh and create credit by giving out loans or promising loan worth 10 lakhs or 20 lakhs, they cannot do that. They do not create credit is very important cooperative banks; it is another difference between commercial banks and cooperative banks next.

So, now, imagine a group of poor farmers found the cooperative society here, comes the catch. You cannot create the credit and make a lot of money you may be mistake n p s may be there, but at least there is a possibility to making a lot of money because out of one lakh create a loan of ten crores or ten lakhs. So, I earned interest on that may be couple of loans have failed, but most of them bring home some interest over a period of time. So, how would cooperative societies run? First of all cooperative societies are not share capital it cannot be registered in the Bombay stock market or whatever and raise primary shares, primary capital. There all your and my money put together how much money will it to be if the poor people in the rural areas of India forming them here comes the catch.

So, they are (()) the capital on the basis of which they operates will be very be small. The need any one individual may be equal to the total of money we collected if one person borrows that money today for two years three years or whatever now what you will have any help from that (()) for two years, three years till he returns and the danger is if he fails to return [FL] cooperative society [FL]. So, here comes the most important issue, how do cooperative banks therefore function, how do they function. So, if

you go through the literature what you find I am looked up much data. Cooperative bank receive financial and other help also other help can be like advisory help, help regarding training how would you run your bank. A bunch of illiterate people they do not know how to run the bank they have to be thought and trained mid literates perhaps to some extent. But I will tell you what they do, if they run well. They often hire managers like commercial banks to run there, but they are paid people. They are not owners of the bank, they are paid people like manager, they are hired like ownership companies hire managers you know that like say two persons have created a partnership company, they can hire people who are not the owners, but paid employee of that company.

So, cooperative banks receive financial and other help from here comes RBI, NABARDS, Central government, State governments and other cooperative banks very important. Some cooperative banks are doing very well. There comes the most interesting issue often cooperative banks helps other cooperative banks, but that would not be to much some. The bulk of the help comes in India from RBI, NABARD, of course, state government and sometimes central government allocates some funds in a budget. Now how does the money reach, this is very interesting. I think that entire root for money to reach may be NABARD also the same think, they do not directly give to the village primary agriculture credit society [FL] or they are given at the district level they do not give go and contact central cooperative banks. In the case of rural credit and then give the money [FL] loan, no, they were very formal bureaucratic structure.

Most probably what I have understood is that the money is not given to them. But they are given to the state governments who in turn allocate to the state cooperative banks or state land development banks who in turn go and give the money to the central cooperative banks, and then from the district level the central cooperative banks disperse the money among the village level banks which are called primary agriculture credit societies or incase of long-term credit which you just saw. In case of long term credit what they do is they go to either to the central land what land development banks or land developments banks or the branches of primary land development banks or branches of state land development banks.

You see what I am saying money is not given to the particular in the village level banks directly, who disperse loans to the members. Money cannot comes like grandfather [FL] grandfather [FL] among children then they give it to their children, and then they use it.

So, the grandchildren do not receive the money directly very bureaucratic alright and of course, NABARD, does a lot here. So, what happens compare to commercial banks, the borrowing part from RBI in relation to their deposits which every member has contributed, the contributed fund, the contribution and the deposits that they have from the bank customers, the borrowed money unlike commercial banks which you have seen data or you haven't seen you will see data.

The borrowed money of cooperative banks is much bigger than what their money is in terms of deposits. Whereas in case of commercial banks, the deposits or the bulk out which investment take place credits are created loans are given etcetera and they have some borrowing which is a fraction of the total deposit that they collect. In case of cooperative bank, it is the [FL], the deposits are very small not sufficient at all for yours and mine need from that society that we have formed. So, we ask external agencies to give us help, and various roots various external agencies give us help, but via one root.

Most probable either to the state level cooperative banks directly down or first state government then from the state government to the state cooperative banks both in rural credit short-term and long-term credit. And in case of urban cooperative banks then they go to the district level from the district level it goes to the village level. Therefore, if you accepted this point, therefore RBI when it comes or whoever controls them the state government, the rules and regulations are slightly different regulatory measures the slightly different compare to commercial banks. Commercial banks they have CRR, SLR. In case of cooperative banks they have deposits, so there will be CRR, SLR, but very low number, like CRR is three percent. Because [FL] cooperative banks CRR is three percent [FL], but SLR may be very high, because that is just not cash, that is forcing cooperative banks to invest in securities etcetera build up an asset accumulation of assets.

If I force you to invest a valuable, so you go by gold, you go by shares, certificate to create an asset that is SLR essentially not keeping just cash. You are forced to invest, so SLR is high, but CRR is very low like three percent something. But one interesting thing, they have in addition to commercial banks is that they have to maintain a desired ratio between their own funds which are the members funds and the deposits whatever they have collected from the customers who open their accounts there and the total borrowings they have to maintain a ratio. Like the total borrowings cannot be more than

three times, total borrowings of a cooperative banks cannot be more than three times your own funds, your own contributions etcetera, perhaps deposits also. Or [FL] deposits are exempted deposits are looked up on as some sort of a borrowed money somebody insists. So, the members money on the basis of which cooperative society was founded and the borrowed money will have a critical ratio maintain not more than three times that not more than four times that. So, they have an extra regulatory restriction on them this is the very important think to understand [FL].

Next, since, your evaluated is not yet here. I can keep on talking this is what I have already told you, let me repeat. Cooperative banks are under the direct control of the state governments, quality banks are under the direct control of the state governments, instead of the RBI. I told you cooperative society, if you have to found a cooperative society if you have to get a licenses or gets registered. The registration is done by the state cooperative department, but in case of commercial banks where do you get the license, in case of commercial banks where do you get the license. If you want to found the if you want to open a commercial bank tomorrow, where would you get the licenses whom would you approach - RBI.

So, now, you can see who is the direct controller of the these banks cooperative banks, the state government, because they issue the licenses or does the registration. So, cooperative banks are under the direct control of the state governments instead of RBI. Under cooperative societies act, there is an act cooperative societies act. State government audit supervise and periodically inspect these banks, just what RBI does with respect to commercial bank, just what RBI does with respect to commercial bank. State cooperative banks audit there accounts supervise them and periodically inspect them. In addition district level banks are supervise and control by the state level banks and district level banks in turn control and supervise the village level banks fascinating stuff.

Do you see, how complex it is? State governments does the work of a RBI here. In addition who is my like grandfather audits and supervise my father activities. My father audits the and supervises and periodically visits my home to see what I am doing. In addition the state government personnel also comes into our houses. All of our houses and audits and supervises and regulate them. It is very very different than commercial

bank. It is very bureaucratic structure upper level lower level business, do you understand what I am saying. [FL] culture is very much here kind of a thing.